

Financing business deals means mastering a delicate dance



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When Mainstream Renewable Power Ltd. was asked to help IKEA Canada build 20 wind turbines in Alberta, Saad Qais knew that for him, it would be all about the money.

“These are capital-intensive projects, and most people in our situation will go for bank financing,” says Mr. Qais, who is vice-president of corporate finance for Chicago-based Mainstream, which has developed similar projects in Europe, South Africa and Chile.

Developing means finding the money – typically for a project of this size, in the tens of millions. “First you look for debt financing, then for equity,” he says.

To arrange corporate financing, you need a solid strategy. This is true whether you’re raising less than \$1-million to build a family business, \$100-million to expand a plant or \$1-billion or more for a takeover bid.

Typically it takes at least six months to a year or longer to line up corporate financing, depending on the deal or project. It’s also critical to determine what kind of financing is needed – what kind of lenders, how the financing will be structured, the terms and guarantees and more.

“There’s a lot of time spent in coming up with an agreement that works for both the borrower and the lender,” says Jennifer Legge, a partner in the corporate group at the law firm Stikeman Elliott LLP in Toronto. “The borrower wants to be able to live within the parameters of an agreement; the lender wants security.”

The particulars of each corporate financing arrangement depend on the size and type of business, its management and ownership, the type of financing and, most importantly, the future.

“Each company has its own strategies, but you start to see some similarities,” says Dana Maloney, area vice-president for Toronto commercial, Bank of Nova Scotia.

Lenders will provide advice to borrowers on how to structure their corporate financing so the terms are realistic and payments can be made on time. But it’s up to companies to give the lenders an idea of how the funds will be best used.

“We provide financial advice. They [companies seeking financing] are the business experts; they know their businesses better than we will,” Mr. Maloney explains.

A prospective borrower should come to a lender prepared with up-to-date financial statements, including the most recent tax statements, he says. Companies should also be prepared to discuss their business strategy, “who their clients are, what opportunities they see.”

Then the bank considers growth. “You want to know what a business will look like in the next 12 months,” Mr. Maloney says.

Lenders will want some analysis of the business strategy from an outside party, Mr. Qais says. “The banks need everything to be independently verified, so it’s not coming from a biased view.”

Lenders want to make sure the business is stable, says Ian Macdonnell, managing director of Crosbie & Company Inc. investment bankers in Toronto. “They want to know they’re going to get their principal back and get paid. The other thing they’re looking for is a management team they can be comfortable with.”

Borrowing from a bank is easier for businesses with tangible assets such as manufacturers, Ms. Legge says. This is commonly known as asset-based lending; corporate finance experts refer to it as ABL.

“It will really depend on the maturity of the business. Most of the time when businesses are starting out it’s difficult to get financing,” Ms. Legge says. “A manufacturing business will have inventory and receivables and will often go for a specific type of credit facility from the lender.”

A credit facility is a revolving type of loan. Each month, the borrower reports to the bank on its receivables and the lender offers credit based on the monthly report. Lenders also look at a company’s “run” or “burn” rate – what the company spends to keep running smoothly month-to-month.

Financing is different when the amount needed reaches higher levels – for example, when there’s a takeover bid. “In those circumstances, you’re not

necessarily looking at receivables. The borrower is looking for a big chunk of money and maybe venture capital [investors looking to buy a percentage of the company],” Ms. Legge says.

The loan in these large-amount situations will likely be for a fixed term, with lenders looking at the company’s cash flow over the life of the loan and, possibly, year-to-year for several years.

Large-business financing is also done through syndicated loans. A group of lenders will pool their money, with one lender acting as the agent for the rest.

As a company’s capital requirements grow, it’s more likely to seek equity partners as well as debt financing, says Geoff Taber, a partner at Osler, Hoskin & Harcourt LLP in Toronto. When the need climbs above \$100-million, companies usually also go to the bond market for funds, he adds.

Corporate financiers need to build three common elements into every loan agreement, no matter the size, Ms. Legge says. These are: representations and warranties (facts that the borrower provides about the business); covenants or promises (how the company intends to use the funds); and agreement on what happens if the borrower can’t make its payments and the lender wants to call in the loan.

Corporate finance experts agree that Canadian banks are relatively cautious, and that while this used to be considered a weakness, since the 2008 economic crash it’s now a strength.

“Canadian banks being more conservative in nature helps us as well,” says Mr. Qais. “Their approach is more sophisticated [than in many other countries]. They make sure all the t’s are crossed and the i’s are dotted.”